Supreme Court, U.S.
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No.

In The

Supreme Court of the United States

October Term, 1998

JULIAN P. KORNFELD,

Petitioner

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

On Petition for Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

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PETITION FOR WRIT OF CERTIORARI

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QUESTIONS PRESENTED FOR REVIEW

I. Is there a denial of due process of law when the United States Court of Appeals for the Tenth Circuit ("Court of Appeals") totally ignores: (i) the evidence in the record; (ii) the decisions of this Court; (iii) its own decision without any attempt to either distinguish the prior decision or overrule it; (iv) the decisions of four other Circuits without any attempt to either distinguish them or disagree with them; and creates its own facts not in the record, in order to render a result oriented decision?

II. Can the Court of Appeals ignore this Court's distinctions between *Commissioner v. Court Holding Co.*, 324 U.S. 331 (1945) ("*Court Holding*") and *Cumberland Public Service Corp. v. Commissioner*, 338 U.S. 451 (1950) ("*Cumberland*"), in order to render a result oriented decision?

III. Can the Court of Appeals ignore the principle enunciated by it in *Associated Wholesale Grocers, Inc. v. United States*, 927 F.2d 1517 (10th Cir., 1991) ("*Associated Wholesale Grocers*") without either overruling itself or distinguishing this case, in order to render a result oriented decision?

IV. Can the "step transaction doctrine" of Federal income tax law be applied where no steps in a transaction are legally binding upon any of the parties?

V. Do "intentions", "expectations" and/or "motivations", absent a binding legal obligation to perform an act or refrain from an act, allow the Internal Revenue Service and/or the courts to restructure a transaction to impose a greater tax liability?

VI. In a fully stipulated case, may either a trial court or an appellate court create "additional facts" to obtain a particular result?

LIST OF PARTIES

The names of all parties to the proceeding in the court whose judgment is sought to be reviewed appear in the caption of the case. There is no parent or subsidiary company of any party.

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Appendix 2 — Order of the United States Tax Court With Respect to Motion to Vacate Decision Dated November 18, 1996 ..... 18a

Appendix 3 — Opinion of the United States Court of Appeals For the Tenth Circuit Decided March 3, 1998 ..... 21a

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OPINIONS BELOW

1. Memorandum Opinion of United States Tax Court ("Tax Court"), *Julian P. Kornfeld v. CIR*, Docket No. 13169-95, T.C. Memo 1996-472, dated October 22, 1996, 72 TCM 1062, attached as Appendix 1.

2. "Order" of Tax Court with Respect to Motion to Vacate Decision and Motion for Reconsideration of Opinion, United States Tax Court, dated November 18, 1996, attached as Appendix 2.

3. Decision of Court of Appeals, dated March 3, 1998, 137 F.3d 1231, 98-1 USTC ¶50,241, attached as Appendix 3. ("Opinion")

4. Order of Court of Appeals denying Petition for Rehearing dated April 27, 1998, attached as Appendix 4.

STATEMENT OF BASIS FOR JURISDICTION

The Court of Appeals rendered its judgment on March 3, 1998. A Petition for Rehearing was timely filed on April 9, 1998. Rehearing was denied on April 27, 1998. Jurisdiction of this Court is invoked under 28 U.S.C. §1254(1).

STATUTES INVOLVED

A. The pertinent part of the Fifth Amendment to the United States Constitution set forth below:

"No person shall be ... deprived of ... property, without due process of law...."

B. Internal Revenue Code of 1986, 26 U.S.C. §167(a) as follows:

"There shall be allowed as a depreciation deduction a reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)--

(1) of property used in the trade or business, or

(2) of property held for the production of income."[1]

STATEMENT OF THE CASE

A. ISSUE.

This case involves the question of whether Petitioner, Julian P. Kornfeld ("Julian"), may, for federal income tax purposes, take a deduction for amortization of

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[1]This case involves the deduction for amortization of a purchased life estate in bonds. Sec. 167 does not use the word "amortization", but the courts have interpreted Sec. 167 to include "amortization" as well as depreciation. *Bell v. Harrison*, 212 F.2d 253 (2nd Cir., 1954); *W. N. Fry*, 283 F.2d 869 (6th Cir., 1960); *A. B. Gist*, 423 F.2d 1118 (9th Cir., 1970). There is no dispute between the parties that amortization, if otherwise allowable, is within the scope of Sec. 167.

a life estate in bonds, which were purchased jointly by Julian, as life tenant, and his two adult daughters, Meredith Kornfeld "(Meredith") and Nancy Kornfeld "(Nancy") and secretary, Pat Permenter ("Permenter"), as remaindermen.[2]

B. FACTS.

(1) Julian has been a tax attorney for 35 years and, in addition to a law degree, holds the degree of Master of Laws in Taxation from New York University. Supp. Stip., Doc. 15, ¶66.[3]

(2) Before he entered into the transactions at issue in this case, Julian independently researched the law in effect at that time, as to whether an amortization deduction would be allowed for a purchased life or term estate. Supp. Stip., Doc. 15, ¶¶67-78.

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[2]The Tax Court has consistently held that a purchased life or term estate is amortizable even if the underlying property is not. *Lomas Santa Fe, Inc. v. Commissioner*, 74 T.C. 662 (1980); *Gordon v. Commissioner*, 85 T.C. 309 (1985); *Richard Hansen Land, Inc. v. Commissioner*, T.C. Memo 1993-248 65 TCM 2869. But in this case the Tax Court held, utilizing the "step transaction doctrine", that Julian did not really purchase a life estate but bought 100% of the bonds and gifted the remainder interests to his children and secretary. This erroneous conclusion was reached by the Tax Court because Julian made gifts of money to his children and Permenter close in time to their payment for their proportionate interest in the bonds.

[3]References are to the Record on Appeal.

(3) Subsequent to the completion of such research, and in conformity to what he concluded to be the law, Taxpayer, Julian, Meredith, Nancy and Permenter entered into contractual agreements to jointly purchase securities, whereby Julian would purchase a life estate and Meredith, Nancy and Permenter would purchase remainder interests in the securities.. Stip., Doc. 14, ¶9; ¶28; ¶35; ¶44..

(4) At the time of execution of the first agreement, Meredith was 27 years of age and Nancy was 22 years of age. Stip., Doc. 14, ¶14. Permenter was age 48. Stip., Doc. 14, ¶37.

(5) Pursuant to such agreements, Julian, Meredith, Nancy and Permenter did in fact jointly purchase bonds from Prudential Securities, with Julian purchasing a life estate and Meredith, Nancy and Permenter purchasing remainder interests. Stip. Doc. 14, ¶17.

(6) Julian made cash gifts to Meredith, Nancy and Permenter. Stip., Doc. 14, ¶25; ¶27.

(7) The time interval between the cash gifts and the closing dates of all bond joint purchases was between five (5) and fifteen (15) days. Stip. Doc. 14, Ex. 83-CE.

(8) Meredith, Nancy and Permenter deposited the cash gifts in their own separate bank accounts. Stip. Doc. 14, ¶27; Supplemental Stip., Doc. 15, ¶79.

(9) Each of Julian, Meredith, Nancy and Permenter issued their own separate checks to Prudential Securities on their own separate bank accounts for their proportionate part of the purchase price of the bonds before the closing date of each bond purchase. Stip., Doc. 14, ¶23; Supp. Stip., Doc. 15, ¶84. Doc. 14, Ex. 83-CE.

(10) None of Meredith, Nancy or Permenter were under any legally enforceable agreement or obligation to utilize Julian's gifts of cash to purchase their interests in the bonds. Supp. Stip. Doc. 15, ¶135; ¶137.

(11) Each of Meredith, Nancy and Permenter had sufficient assets of their own to pay for their proportionate part of the jointly purchased bonds. Stip., Doc. 14, ¶¶53, 59, 60; Supplemental Stip., Doc. 15, ¶¶92, 93, 94, 97, 98, 99, 100, 101, 102.

C. BASIS FOR FEDERAL JURISDICTION IN THE COURT OF FIRST INSTANCE.

When the Internal Revenue Service issues a notice of deficiency in tax, a taxpayer may petition the United States Tax Court for a redetermination of the deficiency. IRC §6213(a). The United States Courts of Appeal have exclusive jurisdiction to review the decisions of the Tax Court. IRC §7482(a)(1).

D. REASONS RELIED ON FOR ALLOWANCE OF THE WRIT.

Although this case does not involve the death penalty, abortion rights, freedom of speech or any other issues that today will directly impact upon millions of citizens of this nation, it does involve a denial of due process of law through ad hoc result oriented decision making which undermines the due process requirement of "fairness". This judicial concept manipulation is totally unsupported by the evidence, all of which was stipulated.[4]

The judicial criteria in this case was the "step transaction" doctrine[5]; which is composed of three separate

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[4]"...so is it a violation of due process to convict and punish a man without evidence of his guilt." *Thompson v. City of Louisville*, 362 U.S. 203, 206 (1960). While this is not a criminal case, the actions of the Tax Court and Court of Appeals are no less a denial of due process as they have deprived the Petitioner of his property without evidence.

[5]Under this doctrine, by "'linking together all interdependent steps with legal or business significance, rather than taking them in isolation, federal tax liability may be based upon a realistic view of the entire transaction'". *C.I.R. v. Clark*, 489 U.S. 726, 738 (1989) (Emphasis supplied)

alternative theories, the "binding commitment" test[6]; the "interdependence test"[7]; and the "end result" test.[8]

It involves ad hoc decision making by the judiciary entrusted and empowered to uphold the laws of this nation.[9] If the laws are ignored by judges seeking to

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[6]Under the "binding commitment" test, there must be a binding commitment to take later steps in the transaction. *Commissioner v. Gordon*, 391 U.S. 83, 96 (1968). The stipulated facts here are that none of Meredith, Nancy or Permenter were legally obligated to use Julian's cash gifts for their share of the cost of the bonds. Thus, there was no "binding commitment".

[7]Under the "interdependence test", the inquiry is whether "the steps were so interdependent that the legal relations created by one transaction would have been fruitless without a completion of the series." *Associated Wholesale Grocers*, 927 F.2d 1517, at 1527. (Emphasis supplied) But the Court of Appeals acknowledged in this case that "...the gifts could stand on their own without relation to the investments..." 137 F.3d 1235. Thus, there was no "interdependence" of steps.

[8]Under the "end result" test, there must be a "prearranged" plan. *Greene v. U.S.*, 13 F.3d 577, 583 (2nd Cir., 1994). There is no evidence in this case of a "prearranged plan."

[9]This Court has severely criticized "ad hoc" decision making and/or "result oriented" decision making. *Arkansas Educ. Television Com'n. v. Forbes*, _____ U.S. _____, 118 S. Ct. 1633, 1644 (1998); *Leavitt v. Jane L.*, 518 U.S. 137, 145 (1996); *Eu v. San Francisco County Democratic Cent. Committee*, 489 U.S. 214, 234 (1989); *Hilton v. Braunskill*, 481 U.S. 770, 783 (1987); *U.S. v. Paradise*, 480 U.S. 149, 173 (1987); *McKaskle v. Wiggins*, 465 U.S. 168, 194 (1984); *Plyer v. Doe*, 457 U.S. 202, 244 (1982); *Engle v. Isaac*, 456 U.S. 107, 144 (1982); *Coopers & Lybrand v.*

achieve a result they desire, then there is a breakdown in our legal system which will affect all of the citizens of this nation. Both the Tax Court and the Court of Appeals have ignored the stipulated record, the decisions of this Court, the decisions of other Circuits, and even the decision of the Court of Appeals itself in its only decided case on the issue. Thus, there is both a conflict between the Court of Appeals and other Circuits; and the Court of Appeals has departed so far from stare decisis that it has denied Petitioner due process, which requires this Court to exercise its supervisory powers.

> "The vague contours of the due Process Clause do not leave judges at large. [fn4] We may not draw on our merely personal and private notions and disregard the limits that bind judges in their judicial function. Even though the concept of due process of law is not final and fixed, these limits are derived from considerations that are fused in the whole nature of our judicial process." *Rochin v. California*, 342 U.S. 165, 170 (1952)

This Court should remain vigilant to assure that this is still a country governed by laws rather than men and women.

Livesay, 437 U.S. 463, 476, n.28 (1978); *Saxbe v. Sustos*, 419 U.S. 65, 84, n.4 (1974); *Marcus v. Search Warrants of Property*, 367 U.S. 717, 731-2 (1961); *Irvine v. People of California*, 347 U.S. 128, 147 (1954).

1. THE TAX COURT AND THE COURT OF APPEALS HAVE DISREGARDED THE STIPULATED FACTS AND CREATED THEIR OWN FACTS TO REACH THE DESIRED RESULT WHICH DENIES PETITIONER DUE PROCESS OF LAW.

There is no evidence in the fully stipulated record of a "binding commitment" of any of Meredith, Nancy or Permenter to utilize Julian's gifts to pay for their purchase of their remainder interests in the bonds.[10] There is no evidence in the fully stipulated record that Julian's gifts of cash and Meredith's, Nancy's and Permenter's payments for their remainder interests in the bonds were "interdependent." Further, the Court of Appeals found that ".... the gifts here could stand on their own without relation to the investments..." Opinion, 137 F.3d 1235. There is no evidence in the fully stipulated record of a "prearranged plan."

The Court of Appeals has held that a court may not disregard the facts stipulated by the parties. *U.S. v. Sommers*, 351 F.2d 354, 357 (10th Cir., 1965). And that speculative reasoning will not be indulged in. *Hoerl and Associates, P.C. v. U.S., 996 F.2d 226, 229 (10th Cir., 1993).* But, the Court of Appeals has clearly created additional facts based upon speculation, in order to reach its result oriented decision, where it stated:

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[10]On the contrary, the stipulated fact is that none of Meredith, Nancy or Permenter were legally obligated to utilize the gifts of money to purchase their respective interests in the bonds.

(1) "...it is difficult to conceive that the parties would have made the investments as they did ... in the absence of the gifts taxpayer made." (Emphasis supplied) See Opinion, p. 9 and 10, 137 F.3d 1235. [11]

(2) "...it is difficult to conceive that the parties ... would have agreed to the valuations between life estates and remainders, in the absence of the gifts taxpayer made." (Emphasis supplied) See Opinion, pp. 9 and 10, 137 F.3d 1235.[12]

(3) "Complieity among the parties is further supported by the following: ... there is no external manifestation of their separate ownerships (as would be the case of recorded real estate deeds specifying term interests) to permit marketing of a limited interest to outside parties." See Opinion, p.11, 137 F.3d 1235.[13]

Even under the step transaction doctrine of federal

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[11]Yet one of the stipulated facts was that each of Meredith, Nancy and Permenter had sufficient assets of their own to pay for their proportionate part of the jointly purchased bonds.

[12]The valuation of life estates and remainders in this case was based upon the IRS's own tables. The IRS never raised an issue that reliance on its tables was an improper methodology.

[13]The Court of Appeals can only speculate with respect to the above quoted statement. There was no stipulation one way or another with respect to manifestation of separate ownerships. Furthermore, there is no stipulation one way or another that term interests in real estate can be marketed to outside parties, even assuming some external manifestation.

tax law, courts may not invent steps that did not happen. *G. M. Trading Corp. v. Commissioner*, 121 F.3d 977, fn.2 (5th Cir., 1997).

The fact that the Court of Appeals rested its decision on what it "conceived" and not on evidence in the record should be clear to this Court that the decision here was purely result oriented. Just as in *Thompson v. City of Louisville*, supra, Note 4, a decision not based upon evidence is a denial of due process.

2. THE IGNORING OF STARE DECISIS DENIES PETITIONER DUE PROCESS.

"The fundamental requirement of due process is the opportunity to be heard 'at a meaningful time and in a meaningful manner'." *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976), citing *Armstrong v. Manzo*, 380 U.S. 545, 552. (Emphasis supplied)

> "For when a person has an opportunity to speak up in his own defense and when the state must listen to what he has to say, substantively unfair and simply mistaken deprivation of property interests can be prevented." *Fuentes v. Shevin*, 407 U.S. 67, 81, (1972). (Emphasis supplied)

But if the Court of Appeals totally disregards the Petitioner's arguments made in good faith, there is no "fair play" nor has Petitioner had an opportunity to be heard "in a meaningful manner." If the Court of Appeals disregards all cases cited by Petitioner without any attempt to

distinguish them or disagree with them, then the Court of Appeals has not listened to what Petitioner has had to say. This must be a denial of due process of law because the law was ignored in this case.

What good does it do to be allowed a hearing when stipulated evidence is replaced by court speculation, and what Petitioner had to say was totally ignored?

That is what has happened in this case. The Tax Court disallowed the amortization deduction because it believed that there was an "expectation" that gifted monies would be used by Julian's adult children and Permenter to purchase their proportionate interests in the bonds. Petitioner cited to the Tax Court its own decisions and the decisions of three Circuits and the Court of Claims which all stood for the legal principle that "intentions" or "expectations" are not relevant absent legal obligations on parties to do an act or refrain from exercising their own free will with respect to any transaction. The Tax Court stated at 72 TCM 1065:

> "Finally, petitioner relies heavily on cases involving what he claims to be analogous transactions, especially those dealing with gifts of stock to a charity followed by a redemption of such stock by the corporation. We dealt at some length with these cases and cases involving seemingly analogous situations in *Gordon v. Commissioner*, 85 T.C. at 327, and concluded that such cases 'are sufficiently distinguishable in terms of their factual context and the issue involved

> so as not to furnish any significant guidance to our decision herein'. We continue to adhere to that view." (Emphasis supplied)

But the Tax Court in *Gordon* didn't "deal at some length with these cases." In *Gordon* the Tax court stated at 85 T.C. 326:

> "Petitioners cite cases in which courts have refused to recharacterize gifts of corporate stock to charitable foundations immediately before the redemption of the shares....[14], we think that, while somewhat analogous, these cases are sufficiently distinguishable in terms of their factual context and the issue involved so as not to furnish any significant guidance in reaching our decision herein." (Emphasis supplied)

The "issue involved" was whether the "intentions" and/or "expectations" of the taxpayer allowed the Service and/or the Tax Court to restructure the transaction from what actually occurred into something else. There was no analysis by the Tax Court of the gift/redemption cases in either *Gordon* or this case. And yet those cases deal with the exact same issue!

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[14]In *Gordon* the petitioner cited only one Circuit decision and one Tax Court decision. Petitioner here cited to the Tax Court four (4) of the Tax Court's own decisions and three decisions of the Circuits and one of the Court of Claims. See Argument 6, infra.

Petitioner cited to the Court of Appeals cases from the Second, Fifth and Fourth Circuits and the Court of Claims that "expectations", "intentions" and the like are not dispositive in a case of this nature, absent a binding legal obligation on the parties to do an act or refrain from doing an act. See Argument 6, infra. The Court of Appeals ignored all of these cases.

While the Tax Court did not use the words "step transaction" in its opinion, it impliedly did so by recasting the transaction, from one in which Julian bought a life interest in bonds and Meredith, Nancy and Permenter bought the remainder interests, into one where Julian bought the entire property interest in the bonds and gave away the remainder interests. Thus, Petitioner cited to the Court of Appeals its only opinion on "step transaction", *Associated Wholesale Grocers*, which utilized the "interdependence test" as to whether the step transaction doctrine applied. See Argument 4, infra.

The Court of Appeals found that "the gifts here could stand on their own without relation to the investments ...." Opinion, p.9; 137 F.3rd 1231, 1235. Since the gifts could "stand on their own without relation to the investments", there was no "interdependence" of steps in this case. The Court of Appeals thus ignored its own principle of law as set forth in *Associated Wholesale Grocers*.[15]

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[15]This Court has also enunciated the principle of "binding commitment" with respect to "step transactions." *Commissioner v. Gordon*, 391 U.S. 83 (1968) ("...if one transaction is to be characterized as a 'first step' there must be a binding commitment

In his Petition for Rehearing With Suggestion for Rehearing En Banc, Petitioner brought to the attention of the Court of Appeals that it had failed to apply the principles of *Associated Wholesale Grocers* to this case. Eighteen (18) days after the Petition for Rehearing was filed, the Court of Appeals issued a one line denial. See Appendix 4.

This Court stated in *Missouri v. Jenkins*, 495 U.S. 33, 46, n. 14, (1990):

> "A petition for rehearing is designed to bring to the panel's attention points of law or fact that it may have overlooked. Fed. Rule. App. Proc. 40(a). The panel is required to consider the contentions in the petition for rehearing, if only to reject them."

It is obvious that the Court of Appeals did not consider the contentions of the Petition for Rehearing because the Court of Appeals totally ignored its own decision and legal principle set forth in *Associated Wholesale Grocers*.

Yet, in *Foster v. MCI Telecommunications Corp.*, 773 F.2d 1116 (10th Cir., 1985), at 1117; this same Court of Appeals stated:

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to take the later steps". 83 U.S. 96). The Court of Appeals believes this Court's "binding commitment" test is confined to the facts in the *Gordon* case. 927 F.2d 1517, 1522, n.6.

> "... MCI petitioned the court to rehear this case in order to consider issues raised in the appeal but not discussed in the Court's Order and Judgment and also to reconsider the Court's ruling."
>
> "In its petition for rehearing, defendant properly points out that this court failed to address an issue legitimately raised in the briefs. Therefore, the petition for rehearing is granted and the opinion is modified as follows:" (Emphasis supplied)

In this case Petitioner devoted ten (10) pages in his Brief-In-Chief to the Court of Appeals to the legal arguments that (1) the step transaction doctrine does not apply where there is a valid gift preceding further transactions; (2) Julian's motives for making the gifts are irrelevant; (3) Julian lost dominion and control of the gifted monies when Meredith, Nancy and Permenter deposited them to their own separate bank accounts; and (4) "expectations" and "intentions" are irrelevant because there was no legally binding obligation on Meredith, Nancy and Permenter to use the gifts for the purchase of bonds. These arguments, which included substantial authority, were not addressed at all in the Opinion.

While Petitioner has had an "opportunity" to be heard, he has not been heard in a "meaningful manner." When the Court of Appeals will not even consider arguments based upon substantial authority from its own Circuit, other Circuits and the Supreme Court, if nothing more than to say "we disagree" or "these cases are

distinguishable", there has been no fair play. There has been a denial of due process of law!

3. THE TAX COURT AND COURT OF APPEALS IGNORED THE DISTINCTIONS MADE BY THIS COURT BETWEEN *COURT HOLDING* AND *CUMBERLAND*.

The Tax Court cited *Court Holding* and *Cumberland* at p.7 of its Opinion, 72 TCM 1064, but failed to apply the distinctions set forth in those cases to this case. The Court of Appeals cited *Court Holding* at 137 F.3d 1234, without any analysis and totally ignored *Cumberland*.

In *Court Holding*, a decision for the IRS, a corporation entered into a contract to sell its only asset (a parcel of real estate) to a buyer and received a down payment. Upon learning that a sale by the corporation would produce a taxable gain at the corporate level and another tax on the distribution of the proceeds, the corporation distributed the real estate to its shareholders.[16] The shareholders then executed a contract with the buyer on the same terms and conditions as the corporation had agreed to and applied the down payment previously paid to the corporation to the purchase price. The Service took the position that the sale was made by the corporation. The Tax Court agreed.

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[16]Under the Internal Revenue Code in effect at that time, no gain was recognized by a corporation in distributing its assets to shareholders in liquidation.

This Court held that "there was evidence to support the findings of the Tax Court ..." 324 U.S. 333; and that "A sale by one person cannot be transferred for tax purposes into a sale by another by using the latter as a conduit through which to pass title." 324 U.S. 334.[17] In *Court Holding* there was a "done deal" which was then changed for no reason but to avoid taxes.

By contrast, in *Cumberland*, a decision for the taxpayer, the shareholders, "...desiring to save payment of the corporate capital gains tax ...", 338 U.S. 452 (Emphasis supplied), caused the corporation to transfer all of the assets of the corporation to them in liquidation. They then sold the assets to a prearranged buyer waiting in the wings. See Arg. 6, infra. This Court distinguished *Court Holding*; and with respect to the statement in *Court Holding* that "'the incidence of taxation depends upon the substance of a transaction' regardless of 'mere formalisms', and that taxes on a corporate sale cannot be avoided by using the shareholders as a 'conduit through which to pass title'", stated:

> "This language does not mean that a corporation can be taxed even when the sale has been made by its stockholders following

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[17] In *Cumberland* this Court stated that its decision in *Court Holding* "...rested on findings of fact by the Tax Court that a sale had been made and gains realized by the taxpayer corporation." 338 U.S. 453 (Emphasis supplied). In this case all facts were stipulated and the Tax Court made no separate findings of fact. The law is clear that a court may not disregard the facts stipulated by the parties. *U.S. v. Sommers*, supra.

a genuine liquidation and dissolution." 338 U.S. 454.

This case was fully stipulated. The Petitioner did not, as in *Court Holding*, enter into any agreement to buy 100% of the bonds and then change the deal to seek a better tax advantage. On the contrary, just as in *Cumberland*, the Petitioner structured the transaction to take advantage of the favorable provisions of existing law. This Court stated in *Gregory v. Helvering*, 293 U.S. 465 (1935), that "The legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them, by means which the law permits, cannot be doubted."

The *Gregory* case is often referred to as the doctrine of "substance vs. form" or "business purpose apart from tax savings" by virtue of the following:

> "Putting aside, then, the question of motive in respect of taxation altogether, and fixing the character of the proceeding by what actually occurred, what do we find? Simply an operation having no business or corporate purpose — a mere device which put on the form of a corporate reorganization as a disguise for concealing its real character, and the sole object and accomplishment of which was a preconceived plan, not to reorganize a business or any part of a business, but to transfer a parcel of corporate shares to the petitioner. No doubt, a new and valid corporation was created.

> But the corporation was nothing more than a contrivance to the end last described. It was brought into existence for no other purpose; it performed, as it was intended from the beginning it should perform, no other function. When that limited function had been exercised, it was immediately put to death." 293 U.S. 469. (Emphasis supplied)

In this case what "actually occurred" was the purchase of real bonds from a real third party, Prudential Securities. Real money was paid for the bonds by each of the joint purchasers from their own separate bank accounts. Julian parted with dominion and control of the cash gifts.[18] Each party actually owned an interest in the bonds. The Tax Court's decision rested primarily on the time span between the gifts and Meredith's, Nancy's and Permenter's payments to Prudential Securities:

> "The time span between confirmation, payment and closing dates reflected in Ex. 1 to the opinion are such as to indicate that neither Nancy, Meredith nor Permenter <u>had any meaningful opportunity or desire to exercise dominion and control over the funds and elect not to participate in the purchase</u>." 72 TCM 1065 (Emphasis supplied)

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[18]Treasury Reg. §25.2511-2(b); *Estate of Dillingham v. Commissioner*, 903 F.2d 760 (10th Cir., 1990); *Estate of Metzger*, 38 F.3d 118 (4th Cir., 1994).

This language is absolute proof that the Tax Court's opinion was "result oriented". The parties did not have to elect "not to participate in the purchase." Not participating would occur if Meredith, Nancy and Permenter deposited the gifts of cash in their separate bank accounts (which is the stipulated fact) and did nothing. They indeed participated by the affirmative act of writing their own checks to Prudential Securities. Therefore, a fortiori, Meredith, Nancy and Permenter without question exercised dominion and control of their own separate funds.

Furthermore, the Tax Court's opinion, in focusing on the "time span" without any objective parameter as to how much time is sufficient, demonstrates graphically the ad hoc nature of the decision. The time span in this case between Julian's gifts and the closing date of each purchase was between five (5) days and fifteen (15) days.[19] How much time is sufficient? Thirty days? Three months? One year? The law, at least prior to this case, has no "time span" requirement. The Tax Court has refused to draw an objective line, thus perpetuating its ability to continue issuing ad hoc decisions.

4. THE COURT OF APPEALS IGNORED ITS OWN DECISION WITHOUT ATTEMPTING TO EITHER DISTINGUISH IT FROM THIS CASE OR STATE THAT ITS EARLIER DECISION WAS WRONG.

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[19]The checks written by Meredith, Nancy and Permenter to Prudential Securities were all prior to the closing date of each bond purchase.

In *Associated Wholesale Grocers* the Court of Appeals applied the "interdependence test" of the step transaction doctrine stating:

> "Under the 'interdependence test' we focus primarily on the relationship between the steps [citation omitted], and in so doing inquire whether 'the steps were so interdependent that the legal relations created by one transaction would have been fruitless without a completion of the series.'" 927 F.2d 1517, at 1527.

The Court of Appeals stated:

> "Under the express terms of the merger agreement, the legal relations it created were entirely contingent on the continuing force of the reorganization agreement. Thus, the merger agreement would bear no fruit unless the two step series could be completed." 927 F.2d at 1528. (Emphasis supplied)

In contrast, in this case, the steps were not interdependent, but were totally independent, and the Opinion of the Court of Appeals so recognizes at p.9, 137 F.3d 1235, where it states:

> "Although the gifts here could stand on their own without relation to the investments, it is difficult to conceive that the parties would have made the investments as they did .... in

the absence of the gifts taxpayer made." (Emphasis supplied)

Because the gifts could stand on their own, there was no "interdependency of steps"; and the Court of Appeals should have reversed the Tax Court.

By totally ignoring its own decision in *Associated Wholesale Grocers* and the criteria set forth therein, the Court of Appeals has refused to apply the doctrine of stare decisis in order to achieve a particular result. Furthermore, the Court of Appeals engages in speculation as to what the parties would have done absent the gifts, again ignoring its own prior opinion that it will not engage in speculation. See *Hoerl*, supra.

The Court of Appeals cited this Court's decision in *Commissioner v. Clark*, 489 U.S. 726, at 738. But this Court in *Clark* focused on the interdependency of steps. This case does not involve interdependent steps and the Court of Appeals has so acknowledged.

5. THE COURT OF APPEALS, IGNORING THE DOCTRINE OF STARE DECISIS, HELD THAT THIS CASE SATISFIED THE "END RESULT" TEST.

At page 9 of the Opinion, 137 F.3d 1235, the Court of Appeals states that "The instant case would appear clearly to satisfy the 'end result' test." There is no further elucidation of why the instant case would "appear clearly to satisfy the 'end result' test". Even in *Associated Wholesale Grocers*, the Court of Appeals did not set forth any objective factors which are prerequisite to the "end

result test" having application. However, the Second Circuit in *Greene v. U.S.*, 13 F.3d 577 (1994), has clearly elucidated what is necessary for the end result test to apply. The Second Circuit stated:

> "Under the end result test, the step transaction doctrine will be invoked if it appears that a series of separate transactions were prearranged parts of what was a single transaction, cast from the outset to achieve the ultimate result." (Emphasis supplied) 13 F.3d at 583.

But the Second Circuit in *Greene* found no evidence of a prearranged plan stating:

> "* * * There simply is no evidence of a prearranged plan between Greene and the Institute for selling the futures contracts immediately upon receipt. * * * Specifically, Appellant urges that a donation followed by a sale by the donee is really a sale by the donor followed by a donation. In this fashion, the government turns fact into fiction." 13 F.3d at 583 (Emphasis supplied)

By holding that Julian bought 100% of the bonds and made gifts of remainder interests, both the Tax Court and the Court of Appeals turn fact into fiction in order to reach their result oriented decisions. This case was fully stipulated. There is no evidence of a prearranged plan. Only by disregarding the stipulated facts and/or engaging

in speculation can either the Tax Court or the Court of Appeals conclude there was a prearranged plan.[20],[21]

6. THE COURT OF APPEALS, AS WELL AS THE TAX COURT, BASED THEIR DECISIONS ON THE "INTENTION" AND/OR "EXPECTATIONS" OF THE TAXPAYER.

The Tax Court, at p.11 of its Opinion, 72 TCM 1065, based its decision on the expectation of the taxpayer that his children would utilize gifted monies to purchase a remainder interest in the bonds. ("We think that the pattern of the transactions herein unquestionably falls within the 'expectation' parameter".) But *Cumberland* makes it clear that there is nothing sinister about a prearranged plan. From a review of the Court of Claims decision in *Cumberland*, 83 F.Supp. 843, it is clear that the transaction was prearranged from the outset and structured carefully to avoid the *Court Holding* scenario. Indeed, the shareholders of the corporation entered into a contract with the buyer to sell the desired assets even before they actually received them pursuant to the corporate liquidation, the contract stating, inter alia, "Whereas, Vendors expect to acquire [the assets] ...." 83 F.Supp, at 848. That contract was entered into on June 10, 1940; the

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[20]A court may not disregard the facts stipulated by the parties. *U.S. v. Sommers*, supra. Nor may a court engage in speculation. *Hoerl* supra.

[21]Based upon this Court's decision in *Cumberland*, which clearly involved a prearranged plan, a prearrangement is not fatal to the transaction in this case. See 6, infra.

plan of liquidation was adopted on August 13, 1940; the shareholders actually received the assets from the corporation on October 22, 1940; and then conveyed such assets to the buyer on October 24, 1940. It would be difficult to find a greater "prearrangement"!

The Court of Appeals focused upon an "intention" of the taxpayer that the gifted monies would be utilized by the donees to make their purchases ("Finally, although there was no legal requirement that remaindermen would use the gifts of money to purchase the bonds, taxpayer stipulated that his intention in making the gift was to enable to donees to make the purchases.") Opinion, p.11, 137 F.3d 1236.

In utilizing this rationale, both the Tax Court[22] and the Court of Appeals have totally ignored the decisions from the Second Circuit, Fifth Circuit, Fourth Circuit and

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[22]The Tax Court even ignored its own decisions in the charitable gift/stock redemption cases: *Carrington v. Commissioner*, 30 TCM 950 (1971) 952-53 ("the mere expectation that the redemption would be made at a later date or that it had been planned is not enough ..." and "Quite obviously the donees were expected to promptly sell or otherwise dispose of the subjects of the gifts..."); *Robert L. Fox*, 27 TCM 1001 (1968), at 1013 (There can be no doubt that Petitioner expected and anticipated ..." and "... in each case the donor of the property was assured by a 'prior understanding' of the ultimate disposition of the property by the charity donee."); *Phillip Grove v. Commissioner*, 31 TCM 386 (1972), at 395 ("the fact of the repetition of the transaction from 1954 to 1964 tends to support the view that the parties contemplated that all of the stocks might be redeemed.") [Emphasis supplied]

Court of Claims which have held that absent a "binding obligation", "intentions" and "expectations" are immaterial in a case of this nature. See *Carrington v. Commissioner*, 476 F.2d 704 (5th Cir., 1973) ("There is neither evidence of, nor suggestion that, there was a prior obligation on a part of the charity to redeem this stock so that Carrington would regain control of Cardinal."); *Grove v. Commissioner*, 490 F.2d 241 (2nd Cir., 1973) ("If Grove made a valid, binding and irrevocable gift of the corporation's share to RPI, it would be the purest fiction to treat the redemption proceeds as having been actually been received by Grove."); *Dewitt v. United States*, 74-1 USTC ¶9369 (Ct. of Cl., 1974) ("* * * "Prearrangements, understandings or tentative planning between the involved parties which do not involve legal obligations on them to either sell or purchase the gift after it is given, will not invalidate the gift."); *Behrend v. United States*, 73-1 USTC ¶9123 (4th Cir., 1972) [A case where the taxpayers stipulated that they "intended" that there would be a forthcoming redemption of stock when they donated the stock to their own charitable foundation], where the Fourth Circuit stated at page 80,067:

> "Furthermore, the gifts were absolutely perfected before the corporation redeemed the stock, performance of none of the steps was compellable; there was no binding obligation on the parties to carry through any step."

The Court of Appeals totally ignored all of these decisions. It did not attempt to distinguish them; it did not state that they were wrong; it did not state that it disagreed

with the conclusions of these Circuits. It simply ignored the entire argument. It even disregarded its own case of *Dowell v. U.S.*, 553 F.2d 1233 (10th Cir., 1977) where it stated at p. 1238: "Motivation and personal expectations do not destroy the reality and genuineness of a given transaction even in a tax case."

CONCLUSION

This is a case where a taxpayer, a tax attorney, sought to "...decrease the amount of what would otherwise be his taxes by means which the law permits.." *Gregory v. Helvering*, supra. *Commissioner v. First Security Bank of Utah, N.A.*, 405 U.S. 394 (1972), citing *Commissioner v. Newman*, 159 F.2d 848.[23] He was denied that right because both the Tax Court and the Court of Appeals, in order to reach a particular result, totally ignored the stipulated record, the decisions of this Court, other Circuits and even their own decisions. And, most importantly, they created additional facts upon which to rest their decisions based upon "beliefs" and conjecture. "If ever a court was guilty of an unabashedly result-oriented approach, this case is a prime example." *Plyer v. Doe*, 457 U.S. 202, 244 (Mr. Chief Justice Burger, dissenting).

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[23] "Over and over again courts have said that there is nothing sinister in so arranging one's affairs as to keep taxes as low as possible. Everybody does so, rich or poor; and all due right, for nobody owes any public duty to pay more than the law demands: taxes are enforced exactions, not voluntary contributions. To demand more in the name of morals is mere cant." 159 F.2d 850-851.

It is one thing for a taxpayer to lose his case where a court examines the evidence in the record; considers his good faith arguments based on reported decisions, and either distinguishes them or disagrees with the legal conclusions reached by the other courts. It is another thing for courts to totally ignore the evidence in the record, engage in speculation to create additional facts, and ignore the taxpayer's arguments. One can only conclude that the Tax Court and the Court of Appeals reached their decisions on the basis of the result they desired. This is such an egregious departure from what the American system of jurisprudence is based upon as to call for this Court to exercise its supervising powers to reverse the Tax Court and Court of Appeals.

If stare decisis still has meaning in America, this Court should grant certiorari and answer the "Questions Presented For Review" as follows:

1. There has been a denial of due process where the lower courts have (i) ignored the evidence; (ii) ignored the decisions of this Court; (iii) ignored the decisions of other Circuits; and (iv) created their own facts not in the record.

2. The Court of Appeals may not ignore the distinctions pronounced by this Court between *Court Holding* and *Cumberland*.

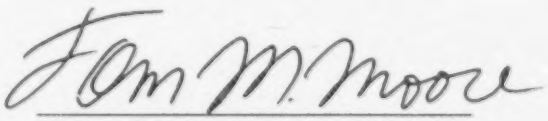
3. The Court of Appeals may not ignore the principles of its prior decision without either overruling it or distinguishing it from this case.

4. The "step transaction" doctrine of federal income tax law may not be applied where no subsequent steps are legally binding upon the parties.

5. "Intentions", "expectations" and/or "motivations" do not allow the IRS or the courts to restructure a transaction to create more tax, absent binding legal obligations on parties to perform acts or refrain from acts.

6. In a fully stipulated case, neither a trial court or appellate court may create "additional facts" to obtain a particular result.

Respectfully submitted,



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APPENDIX 1 — MEMORANDUM OPINION OF THE UNITED STATES TAX COURT DATED OCTOBER 22, 1996

T. C. MEMO. 1996-472

UNITED STATES TAX COURT

JULIAN P. KORNFELD, Petitioner v.
COMMISSIONER OF INTERNAL
REVENUE, Respondent

Docket No. 13169-95. Filed October 22, 1996.

Julian P. Kornfeld, pro se.

Clarke L. Randall, for petitioner.

Elizabeth Downs, for respondent.

MEMORANDUM OPINION

TANNENWALD, Judge: Respondent determined deficiencies in petitioner's Federal income taxes for the taxable years 1990 and 1991 in the amounts of $11,803.00 and $13,122.00, respectively. The sole issue for decision is whether petitioner is entitled to amortize the cost of acquiring a life interest in tax-exempt bonds where others simultaneously acquired the remaining interests.

The case was submitted fully stipulated under Rule 122.[1] All of the stipulated facts, including those contained in the attached exhibits, are found accordingly.

Petitioner resided in Oklahoma City, Oklahoma, at all relevant times, including the time when he filed his petition herein. He filed timely individual income tax returns for 1990 and 1991.

Petitioner is an experienced lawyer, particularly in the fields of business and tax law.[2] He has two daughters, Meredith Kornfeld (Meredith) and Nancy Kornfeld (Nancy), both of whom were adults and college graduates at all relevant times. At those times, petitioner also had a long-time secretary and administrative assistant, Patsy D. Permenter (Permenter) , who

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[1] All statutory references are to the Internal Revenue Code in effect for the years in issue, and all Rule references are to the Tax Court Rules of Practice and Procedure.

[2] The stipulation of facts contains a detailed description of petitioner's experience and of his analysis of the pertinent authorities prior to entering into the transactions involved herein. Petitioner has emphasized the description and the analysis presumably to persuade the Court that his "expertise" should be a significant factor influencing us to arrive at a conclusion favorable to him. Respondent has utilized the description presumably to persuade us that petitioner's tax motivation predominated and should persuade us to decide the instant case in her favor. We consider petitioner's background and analysis peripheral (as to respondent's use of it) and irrelevant (as to petitioner's use of it) to the accomplishment of the task before us, namely, independently to reach our own conclusions based on the stipulated factual elements of the transactions involved.

was also an adult at such times and not otherwise related to petitioner.

Petitioner, acting through a revocable trust of which he and Permenter were trustees, entered into agreements entitled Joint Purchases of Life Estates and Remainder Interests pursuant to which the parties would identify securities to be acquired in which petitioner would have a life estate and the other parties would have interests as indicated by the following:

(1) May 1, 1989, agreement - remainder interests in Meredith and Nancy;

(2) June 19, 1989, agreement - remainder interest in Nancy;

(3) October 31, 1989, agreement - secondary life interest in Nancy and remainder interest in Permenter;

(4) June 15, 1990, agreement - secondary life interest in Nancy and remainder interest in Permenter.

All of the agreements provided that the parties would identify securities for joint investment by executing an agreed form designated by the parties as Exhibit A, that each would pay a proportionate share of the purchase price of the joint investments and that the disposition of any such investments could be made only upon the direction of all parties.

The bonds purchased were tax-exempt bonds and were acquired from unknown third parties through Prudential Bache Securities (Prudential Bache) or from Prudential Bache's own inventory of bonds. Prudential Bache confirmed each purchase involved herein by a confirmation slip addressed to the Julian P. Kornfeld Life Estate, with an Oklahoma City address.

After the purchases, but before the closing dates, petitioner would calculate the value of the respective interests in the bonds that he and the other parties were acquiring. The Exhibits A executed by the parties were dated the same day as the Prudential Bache confirmations. Petitioner's calculations were based upon the actuarial values published by the Internal Revenue Service. The allocations reflected in such calculations are not disputed by respondent.

Based upon the aforesaid calculations, petitioner would furnish Nancy, Meredith, and Permenter with the amounts indicated as their share of the purchase price. This would be accomplished either by check or wire transfer to the respective bank accounts before the closing date of the purchase. During the years in issue, Nancy's bank account was in Minneapolis, Minnesota, Meredith's bank account was in Los Angeles, California, and Permenter's in Oklahoma City, Oklahoma.

With respect to every purchase, the amounts furnished by petitioner were deposited in the bank accounts. Thereafter, and before the closing dates, Nancy, Meredith, and Permenter issued their separate checks to Prudential Bache in the amounts reflected in petitioner's calculations as allocable to the interest each was acquiring. The monthly statements of Prudential Bache for the Julian P. Kornfeld Life Estate indicated the separate receipt of funds from petitioner, Meredith, Nancy, and Permenter.

Neither Meredith, Nancy, nor Permenter was under any legal obligation to utilize the funds received from petitioner to acquire their interests in the purchased bonds. However, they and petitioner intended that the funds would be so used.

Annexed hereto as Exhibit 1 is a schedule reflecting the date and amount of each bond purchase involved herein, the

closing date of Prudential Bache, dates of petitioner's gifts[3] to the other parties, and the dates of payments by petitioner and the other parties.

Petitioner furnished Nancy, Meredith, and Permenter with funds in rounded amounts equal to the payments they made to Prudential Bache. Neither Nancy, Meredith, nor Permenter expended any amount in excess of the funds so furnished to make any part of such payments.

Petitioner filed gift tax returns reflecting the gifts to Nancy, Meredith, and Permenter but paid no tax on account of the unified credit. See sec. 2505. Petitioner reported no other gifts to Meredith, Nancy, or Permenter during the years at issue.

When purchased bonds were redeemed, each party to the agreements received their proceeds based upon the actuarial values thereof published by the Internal Revenue Service. The values are not disputed by respondent.

At issue is the right of petitioner to amortize, ratably over his expected life, his cost of acquiring his life interests in bonds purchased pursuant to joint purchase agreements. Petitioner argues that he purchased his interests and the other participants acted independently in purchasing their interests. Respondent contends that: (1) While, in form, the purchases were by petitioner and the other participants, i.e., petitioner's daughters and secretary, in substance, petitioner purchased the bonds as a whole, retaining life interests for himself and

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[3]The use of the word "gifts" is not dispositive of the subject of the gifts by petitioner, i.e., of funds or interests in the bonds, which is the critical issue herein.

donating the remaining[4] interests to the other participants with the result that (2) petitioner split nondepreciable assets and is not entitled to an amortization deduction. We dealt with the same issue in *Gordon v. Commissioner*, 85 T.C. 309 (1985), in which we sustained respondent's contentions and rejected the taxpayer's claim of an amortization deduction, and in *Richard Hansen Land, Inc. v. Commissioner*, T.C. Memo. 1993-248, where we applied *Gordon* and rejected respondent's contentions and sustained the taxpayer's claim of an amortization deduction in a case involving the acquisition of land.

Initially, we note that the fact that the bonds involved herein were tax-exempt bonds does not operate to deprive petitioner of his claimed amortization deduction. See *Gordon v. Commissioner*, supra at 322 n.6 (citing *Manufacturers Hanover Trust Co. v. Commissioner*, 431 F.2d 664 (2d Cir. 1970), affg. a Memorandum Opinion of this Court).[5] We further note that there is no issue as to the amount of petitioner's claimed amortization deduction if we hold that he is entitled to such deduction.

The basic question is whether or not the transactions were structured in the right way, i.e., whether they were in fact what they appear to be in form. See *Gordon v. Commissioner*, supra; *Hobby v. Commissioner*, 2 T.C. 980, 985 (1943). This

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[4]We use the word "remaining" instead of "remainder" because of the secondary life interest of Nancy in some of the bonds and the fact that the proper characterization of that interest is in question. See infra p. 13.

[5]We note that the extent to which amortization deductions could be taken with respect to tax-exempt income-producing property was not changed by the enactment in 1989 of sec. 167(e). See infra p. 13 and note 6.

is a question that the courts have been faced with many times in a variety of contexts. Compare *Cumberland Public Service Corp. v. Commissioner*, 338 U.S. 451 (1950), with *Commissioner v. Court Holding Co.*, 324 U.S. 331 (1945) (whether a sale was by a corporation or its shareholders). Compare also *Zenz v. Quinlivan*, 213 F.2d 914 (6th Cir. 1954), with *Wall v. United States*, 164 F.2d 462 (4th Cir 1947) (dividend or capital gain on redemption of shares of corporation). We see no need to repeat the underpinnings of that question which we explored in detail in *Gordon v. Commissioner*, supra, and *Richard Hansen Land, Inc. v. Commissioner*, supra. We think it important, however, to recognize, as we did in those cases, that the fact that tax reasons generated the choice of the structure used is not, in and of itself, sufficient to require us to sustain respondent.

Against the foregoing background, we proceed to examine the various elements involved herein, upon which the base resolution of the ultimate factual question, i.e., were there separate purchases of a life interest by petitioner and of the remaining interests by the other parties or was there a purchase of the entire ownership of the bonds by petitioner followed by a gift of the interests in the bonds remaining after petitioner's retained life estate. The burden of proof is on petitioner, Rule 142(a), and that burden is not lessened because this is a fully stipulated case. *Borchers v. Commissioner*, 95 T.C. 82, 91 (1990), affd. 943 F.2d 22 (8th Cir. 1991).

Some preliminary observations are in order. First, we recognize, as we did in *Gordon v. Commissioner*, supra, that the holders of the remaining interests were related to petitioner, i.e., daughters, or closely identified with petitioner, i.e., petitioner's

longtime secretary.[6] While such relationships are not determinative, their existence provides a basis for "skepticism" in accepting the form of the transaction. See *Gordon v. Commissioner*, 85 T.C. at 325-326. Moreover, as we also noted in *Gordon*, the pattern of tax benefits flowing from the transactions involved herein are such as to constitute "a yellow caution signal on our road to decision." Id. at 326.

Second, a substantial portion of the stipulation dealt with assets possessed by the participants other than petitioner during the years at issue. While the values of those assets, particularly those of a corporation owned by the daughters, is not clearly established, it would appear that substantial amounts were involved and petitioner argues that the availability of such assets as a potential source of payment for the remaining interests of Nancy, Meredith, and Permenter in the bonds should be considered in determining whether such interests were independently purchased. We agree with respondent that the availability of such assets is irrelevant to the issue before us. That such assets might have been used does not answer the question of how to characterize the transactions involved herein where the funds used were supplied by petitioner.[7]

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[6]While Permenter was not "related" to petitioner in the same way as his daughters, see secs. 167(e)(5)(B) and 267, we are satisfied that, on the basis of the record herein, her "relationship" should not be treated differently in view of the fact that we have concluded that sec. 167(e) does not impact our conclusion. See infra p. 13.

[7]We note that in *Gordon v. Commissioner*, 85 T.C. 309, 328 (1985), we indicated that the presence of other assets available to the holder of the remainder but not used was a factor unfavorable to the taxpayer's position.

Finally, petitioner relies heavily on cases involving what he claims to be analogous transactions, especially those dealing with gifts of stock to a charity followed by a redemption of such stock by the corporation. We dealt at some length with these cases and cases involving seemingly analogous situations in *Gordon v. Commissioner*, 85 T.C. at 327, and concluded that such cases "are sufficiently distinguishable in terms of their factual context and the issue involved so as not to furnish any significant guidance to our decision herein." We continue to adhere to that view.

Petitioner attaches great significance to the fact that gift tax returns were filed in respect to all the funds provided by petitioner, whereas in *Gordon v. Commissioner*, supra, most of the transfers of funds by the taxpayer to the holder of the remainder interest were not reflected in any gift tax returns. We are not persuaded that this provides a significant basis for distinguishing *Gordon*. Such returns merely reflect the values of the gifts[8] to the recipients which happen to coincide with the amounts of the funds transferred. As far as the returns are concerned, the subject matter of the reported gifts is not stated and is consistent with either gifts of cash or of the remaining interests in the bonds. Moreover, the tax impact of the gifts, i.e., the potential loss, at an indeterminate future date, of a portion of petitioner's estate tax exemption by virtue of the utilization of the unified credit is a far cry from the income tax consequences of the receipt of wages by Hansen in *Richard Hansen Land, Inc. v. Commissioner*, T.C. Memo. 1993-248.

Petitioner's principal argument rests on the absence of any legal obligation on Nancy, Meredith, or Permenter to use the funds provided by petitioner to acquire the remaining

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[8]See supra note 3.

interests. While this is an important element, it is not controlling, as our opinion in *Gordon v. Commissioner*, supra, makes clear. Indeed, as we pointed out in *Gordon*, the freedom of Nancy, Meredith, and Permenter legally to refuse to utilize the funds provided by petitioner to pay for the remaining interests "is of minimal significance where * * * the facts reveal that the entire transaction was set up around the expectation that the joint implementation of the * * * [taxpayer's] investment strategy would occur." *Gordon v. Commissioner*, 85 T.C. at 331 n.16. We think that the pattern of the transactions herein unquestionably falls within the "expectation" parameter.[9] Unquestionably, petitioner was the architect of the investment strategy and orchestrator of its implementation. There is no evidence that there was any advance consultation among petitioner and Nancy, Meredith, or Permenter as to any investment, and the Exhibits A executed by them were uniformly dated the same day as the confirmations from Prudential Bache. The amounts of funds provided from time to time by petitioner to Nancy, Meredith, and Permenter were, within pennies, equal to the amounts of the checks they issued to Prudential Bache; by way of contract, the separate funds of the trust in *Gordon v. Commissioner*, supra, were used albeit to a minor extent. The time spans between confirmation, payment, and closing dates reflected in Exhibit 1 to this opinion are such as to indicate that neither Nancy, Meredith, nor Permenter had any meaningful opportunity or desire to exercise dominion and control over the funds and elect not to participate in the purchases.

In short, we are satisfied that, on the basis of the record as a whole, petitioner, like the taxpayer in *Gordon v. Commissioner*, supra, acquired the entire ownership in the

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[9]Cf. *Muserlian v. Commissioner*, 932 F.2d 109, 113 (2d Cir. 1991), affg. T.C. Memo. 1989-493.

bonds and then divided that ownership by retaining a life interest and transferring the remaining interests to Nancy, Meredith, and Permenter.

In arriving at this conclusion, we recognize that we reached an opposite result in *Richard Hansen Land, Inc. v. Commissioner*, supra. However, the factual circumstances in *Hansen Land* were quite different; in particular, in the case of Richard Hansen, he acquired the remainder interest with funds that he received as taxable income in a transaction whose bona fides were not question by respondent. His wholly owned corporation, whose separateness was also not questioned by respondent, acquired the amortizable term interest, and the Kammerzells utilized their own separate funds.

Concededly, the disposition of cases such as the one before us inevitably involves the difficult task of line drawing. But, as we have previously observed:

> the necessity of drawing lines is part of the daily grist of judicial life and should not influence us to adopt another rule simply to avoid difficulties in application. See *Estate of Lillie MacMunn Stewart [v. Commissioner]*, 52 T.C. 830, 836 (1969), revd. on other grounds 436 F.2d 1281 (3rd Cir. 1971). [*Allen v. Commissioner*, 66 T.C. 340, 346 (1976); fn. ref. omitted.]

In view of our conclusion, we have no need to address the application of section 167(e) in respect to the transactions under the October 31, 1989, and June 15, 1990, agreements and the question whether Nancy's secondary life interest constituted a remainder interest for the purpose of that section. See H. Rept. 101-247 at 1361-1362 (1989); H. Conf. Rept. 101-386 at 625-626 (1989).

In view of the foregoing,

Decision will be entered for Respondent.

EXHIBIT 1 Reflecting Bond Purchases Involved in *Kornfeld v. Commissioner*, docket No. 13169-95

First 1989 Agreement **Purchases May 12—June 20, 1989**

	Bond Purchases	*Purchase Date*	*Face Amount*	*Total Purchase Price*	*Life Estate Allocation*	*Remainder Allocation*	*Closing Date Per Prudential*	*Date of Julian's Gifts to Daughters*	*Amount of Julian's Gifts to Daughters*	*Date of Julian's Payment to Prudential*	*Amount of Julian's Payment to Prudential*	*Remaindermen's Payment Date to Prudential*	*Remaindermen's Payment Amount to Prudential*
1	Hurley Wis School Dist.	5/12/89	25,000.00	25,889.65	22,122.44	M 1,883.61 N 1,883.61	5/26/89	M 5/11/89 N 5/11/89	M 3,500.00 N 3,500.00	5/17/89	36,164.39	M 5/17/89 N 5/18/89	M 3,334.63 N 3,334.62
	Lower Colorado River Authority	5/12/89	20,000.00	19,943.99	17,041.95	M 1,451.02 N 1,451.02	5/26/89	M Above N Above	M Above N Above	Above	Above	M Above N Above	M Above N Above
					Total	M 3,334.63 N 3,334.62							
2	Grand Strand Water	5/23/89	25,000.00	26,148.71	22,343.83	M 1,902.45 N 1,902.44	6/08/89	M 5/24/89 N 5/24/89	M 13,500.00 N 13,500.00	5/24/89	158,503.59	M 5/27/89 N 6/14/89	M 13,495.68 N 13,495.68
	Texas State Water	5/23/89	150,000.00	159,346.25	136,159.77	M 11,593.24 N 11,593.24	6/02/89	M Above N Above	M Above N Above	Above	Above	M Above N Above	M Above N Above
					Total	M 13,495.69 N 13,495.68							
3	Texas State	5/30/89	40,000.00	43,124.96	36,849.85	M 3,137.55	6/12/89	M 6/07/89	M 25,300.00[1]	6/06/89	152,507.62	M 6/09/89	M 3,137.55
	Water					N 3,137.56		N 6/07/89	N 25,300.00[1]			N 6/10/89	N 3,137.56
	Porter County Hospital	5/30/89	25,000.00	25,507.72	21,796.72	M 1,855.81 N 1,855.82	6/08/89	M Above N Above	M Above N Above	Above	Above	M Above N Above	M 1,855.81 N 1,855.82
	Dallas Civic Center	5/30/89	100,000.00	109,845.28	93,861.69	M 7,991.79 N 7,991.80	6/09/89	M Above N Above	M Above N Above	Above	Above	M Above N Above	M 7,991.79 N 7,991.80
4	Lower Colorado River Auth	5/31/89	50,000.00	54,261.67	46,366.06	M 3,947.80 N 3,947.81	6/07/89	M Above N Above	M Above N Above	6/06/89	46,366.56	M Above N Above	M 3,947.80 N 3,947.81
5	Nevada State General	6/01/89	100,000.00	108,910.28	92,358.10	M 8,276.09 N 8,276.09	6/12/89	M Above N Above	M Above N Above	6/06/89	92,358.10	M Above N Above	M 8,276.09 N 8,276.09
			Purchases 3, 4 and 5		Total	M 25,209.04 N 25,209.08							

[1] WIRE TRANSFER

First 1989 Agreement — **Purchases May 12—June 20, 1989**

	Bond Purchases	*Purchase Date*	*Face Amount*	*Total Purchase Price*	*Life Estate Allocation*	*Remainder Allocation*	*Closing Date Per Prudential*	*Date of Julian's Gifts to Daughters*	*Amount of Julian's Gifts to Daughters*	*Date of Julian's Payment to Prudential*	*Amount of Julian's Payment to Prudential*	*Remaindermen's Payment Date to Prudential*	*Remaindermen's Payment Amount to Prudential*
6	Birmingham Civic Center	6/06/89	120,000.00	131,056.00	111,138.11	M 9,958.94 N 9,958.95	6/13/89	M 6/7/89 N 6/7/89	M 15,650.00 N 15,650.00	6/07/89	174,656.97	M 6/09/89	M 15,650.78
	Brownsville	6/06/89	70,000.00	74,902.54	19,917.89	M 5,691.84 N 5,691.84		M Above	M Above	Above	Above	N 6/10/89 N 6/10/89	N 9,958.95 N 5,691.84
					Total	M 15,650.78 N 15,650.79							
7	Intermountain Power	6/07/89	10,000.00	10,762.48	9,050.48	M 811.00 N 811.00	6/14/89	M 6/08/89 N 6/08/89	M 9,061.00* N 9,061.00*	6/07/89	9,050.48	M 6/09/89 N 6/10/89	M 811.00 N 811.00
8	DuPage Ill. Water	6/07/89	100,000.00	108,572.63	92,071.76	M 8,250.44 N 8,250.43	6/14/89	M Above N Above	M Above N Above	6/07/89	92,071.76	M 6/09/89 N 6/10/89	M 8,250.44 N 8,250.43
			Purchases 7 and 8		Total	M 9,061.44 N 9,061.43							
9	Houston Airport	6/20/89	10,000.00	10,799.06	9,157.82	M 820.62 N 820.62	6/27/89	M 6/21/89 N 6/21/89	M 821.00* N 821.00*	6/21/89	9,157.82	M Missing N 6/27/89	M 820.62 N 820.62

* WIRE TRANSFER

Second 1989 Agreement **Purchases June 21—August 18, 1989**

	Bond Purchases	Purchase Date	Face Amount	Total Purchase Price	Life Estate Allocation	Remainder Allocation	Closing Date Per Prudential	Date of Julian's Gifts to Daughters	Amount of Julian's Gifts to Daughters	Date of Julian's Payment to Prudential	Amount of Julian's Payment to Prudential	Remaindermen's Payment Date to Prudential	Remaindermen's Payment Amount to Prudential
1	Albuquerque New Mexico Airport	6/21/89	40,000.00	41,945.74	35,570.82	N 6,374.92	6/28/89	N 6/23/89	N 6,400.00 '	6/23/89	39,674.28	N 6/28/89	N 6,374.92
2	N Austin Muni Authority	8/15/89	10,000.00	10,237.89	8,451.38	N 1,786.51	8/29/89	N 8/16/89	N 1,790.00 '	8/16/89	8,451.38	N 8/18/89	N 1,786.51

' WIRE TRANSFER

Third 1989 Agreement — Purchases October 31, 1989 thru May 4, 1990

	Bond Purchases	Purchase Date	Face Amount	Total Purchase Price	First Life Estate Allocation	Second Life Estate Allocation	Remainder Allocation	Closing Date Per Prudential	Date of Julian's Gifts to N and P	Amount of Julian's Gifts to N and P	Date of Julian's Payment to Prudential	Amount of Julian's Payment to Prudential	2nd Life Tenant Payment Date to Prudential	2nd Life Tenant Payment Amount to Prudential	Remaindermen's Payment Date to Prudential	Remaindermen's Payment Amount to Prudential
1	Memphis County	10/31/89	25,000.00	25,908.00	21,387.05	N 3,863.30	P 657.55	11/31/89	N Missing P 10/31/89	N Unknown P 640.00	10/31/89	21,387.05	N 11/15/89	N 3,863.40	P 11/2/89	P 657.55
2	Birmingham Alabama G O	11/6/89	50,000.00	53,471.33	44,143.15	N 7,974.11	P 1,357.18	11/30/89	N 11/8/89 P 11/8/89	N 8,000.00 P 1,400.00	11/9/89	44,143.15	N 11/17/89	N 7,974.11	P 11/13/89	P 1,357.18
3	San Antonio Water	11/30/89	50,000.00	53,221.31	43,936.66	N 7,936.80	P 1,350.85	12/11/89	N 12/1/89 P 12/1/89	N 8,000.00 P 1,350.00	12/1/89	43,936.66	N Missing	N 7,936.80	P 12/5/89	P 1,350.85
4	New York G O	12/1/89	30,000.00	30,330.00	24,619.69	N 4,918.11	P 802.20	12/11/89	N 12/5/89 P 12/5/89	N 29,500.00 P 5,400.00	12/6/89	24,619.69	N Missing	N 4,918.11	P 12/6/89	P 802.20
	Pinellas FL Sports	12/1/89	15,000.00	15,978.59	12,966.00	N 2,590.00	P 422.47	12/11/89	N Above P Above	N Above P Above	12/6/89	12,966.00	N Missing	N 2,590.12	P 12/6/89	P 422.47
	Oklahoma State Turnpike	12/1/89	50,000.00	55,117.39	44,725.39	N 8,934.50	P 1,457.30	12/14/89	N Above P Above	N Above P Above	12/6/89	44,725.39	N Missing	N 8,934.50	P 12/6/89	P 1,457.30
	Atlanta Dev Authority	12/1/89	50,000.00	53,086.26	43,564.25	N 8,702.55	P 1,419.46	12/14/89	N Above P Above	N Above P Above	12/6/89	43,564.25	N Missing	N 8,702.55	P 12/6/89	P 1,419.46
	Mass Bay Transit	12/1/89	25,000.00	25,171.81	21,237.80	N 4,242.45	P 691.99	12/14/89	N Above P Above	N Above P Above	12/6/89	21,237.80	N Missing	N 4,242.45	P 12/6/89	P 691.99
					Total	N 29,387.61	P 4,793.22									
5	New York G O	12/16/89	50,000.00	53,377.00	43,923.00	N 8,184.93	P 1,360.02	3/5/90	N 2/19/90 P 2/19/90	N 16,840.00 P 2,825.00	2/19/90	43,923.00	N 2/25/90	N 8,184.98	P 2/28/90	P 1,360.02
	Fort Wayne Hospital	2/16/89	25,000.00	26,486.08	21,371.62	N 3,981.60	P 732.86	3/5/89	N Above P Above	N Above P Above	2/19/90	21,371.62	N 2/25/90	N 3,981.60	P 2/28/90	P 732.86
	Burlington VT Electric	2/16/89	25,000.00	25,910.28	20,907.00	N 4,286.34	P 716.94	3/5/89	N Above P Above	N Above P Above	2/19/90	20,907.00	N 2/25/90	N 4,286.34	P 2/28/90	P 716.94
					Total	N 16,852.87	P 2,818.82									
6	San Antonio Water/Sewer	4/4/90	35,000.00	36,130.28	29,777.49	N 5,467.23	P 885.56	4/11/90	N 4/5/90 P 4/5/90	N 5,500.00 P 900.00	4/5/90	29,777.49	N 4/11/90	N 5,467.23	P 4/10/90	P 885.56
7	Princeton, Ind	4/12/90	25,000.00	25,447.12	20,972.76	N 3,850.66	P 623.70	4/23/90	N 4/10/90 P 4/10/90	N 3,850.00 P 625.00	3/10/90	20,972.76	N 4/19/90	N 3,850.66	P 4/17/90	P 623.70
8	State of Mass Gen Ob	4/25/90	20,000.00	20,770.26	17,118.23	N 3,142.95	P 509.08	5/9/90	N 4/25/90 P 4/25/90	N 3,200.00 P 510.00	4/25/90	17,118.23	N Missing	N 3,142.95	P 5/1/90	P 509.08
9	State of Wash Gen Ob	5/4/90	15,000.00	15,809.85	13,155.90	N 2,356.18	P 374.77	5/16/90	N 5/7/90 P 5/7/90	N 2,400.00 P 000.00	5/7/90	13,155.90	5/17/90	N 2,356.18	P 5/8/90	P 374.77

June 15, 1990 Agreement — Purchases June 21, 1990 thru August 16, 1990

	Bond Purchases	Purchase Date	Face Amount	Total Purchase Price	First Life Estate Allocation	Second Life Estate Allocation	Remainder Allocation	Closing Date Per Prudential	Date of Julian's Gifts to N and P	Amount of Julian's Gifts to N and P	Date of Julian's Payment to Prudential	Amount of Julian's Payment to Prudential	2nd Life Tenant Payment Date to Prudential	2nd Life Tenant Payment Amount to Prudential	Remaindermen's Payment Date to Prudential	Remaindermen's Payment Amount to Prudential
1	Illinois Health Facility	6/22/90	35,000.00	34,257.00	28,623.44	N 5,200.55	P 433.01	6/28/90	N 6/28/90 P 6/27/90	N 17,900.00 P 1,500.00	6/28/90	28,623.44	N 6/28/90	N 5,200.55	P 6/28/90	P 433.01
	Springfield Ill. Elec	6/21/90	40,000.00	38,322.50	32,028.72	N 5,819.26	P 484.52	6/28/90	N 6/28/90 P 6/27/90	N Above P Above	6/28/90	32,028.72	N 6/28/90	N 5,819.26	P 6/28/90	P 484.52
	Tarrant County TX Water	6/21/90	45,000.00	45,229.38	37,708.90	N 6,865.82	P 571.66	6/28/90	N 6/28/90 P 6/27/90	N Above P Above	6/28/90	37,708.90	N 6/28/90	N 6,865.82	P 6/28/90	P 571.66
					Total	N 17,885.63	P 1,489.19									
2	Tulsa Airport	8/16/90	5,000.00	5,285.37	4,356.04	N 850.15	P 79.18	8/23/90	N 8/17/90 P 8/17/90	N 850.00 P 80.00	8/17/90	4,356.04	N 8/17/90	N 850.15	P 8/21/90	P 79.18

APPENDIX 2 — ORDER OF THE UNITED STATES TAX COURT WITH RESPECT TO MOTION TO VACATE DECISION DATED NOVEMBER 18, 1996

UNITED STATES TAX COURT
WASHINGTON, D. C. 20217

JULIAN P. KORNFELD,	)	
	)	
Petitioner	)	
v.	)	Docket No. 13169-95
	)	
COMMISSIONER OF INTERNAL REVENUE,	)	
	)	
	)	
Respondent	)	

ORDER

Petitioner having, on November 12, 1996, filed a Motion to Vacate Decision and a Motion for Reconsideration of Opinion (T.C. Memo 1996-472 filed October 22, 1996), after due consideration, it is

ORDERED: That petitioner's motion for reconsideration of opinion is granted in that the opinion is amended by making the following changes:

(1) The last full sentence on page 10 of the opinion is stricken and the following substituted in its place and stead: "although the gift tax returns stated that the gifts were cash gifts, such self-serving labeling is not determinative and its

impact is not significant in light of the other factors discussed herein which cause us to conclude that interests in the bonds themselves were the subject matter of the gifts."

(2) The sentence beginning on the fourth line from the bottom of page 11 of the opinion is stricken and the following is substituted in its place and stead: "We are aware that the parties have stipulated that 'Because of Julian's tax, financial, and business expertise, Meredith and Nancy generally consult with Julian about all major or significant financial transactions.' But such a general description lacks the quality necessary to support the conclusion that there was meaningful advance consultation and exercise of independent judgment by Nancy and Meredith in respect of the specific transactions involved herein, to say nothing of the fact that the stipulation does not include any reference to Permenter. Moreover, we note that Exhibits A executed by petitioner and Nancy, Meredith, or Permenter were uniformly dated the same day as the confirmations from Prudential Bache." It is further

ORDERED: That, except as aforesaid, petitioner's motions are denied.

We are unpersuaded by the litany of decided cases from which petitioner constructs an absolute rule as a divining rod for decision herein, i.e., that the determinative factor is the absence of any legal obligation on the part of Nancy, Meredith, or Permenter to utilize the cash received from petitioner to participate in the bond transactions. In taking this position, petitioner fails to recognize that the situation herein is one which, as we stated in our opinion, involves the "difficult task of line drawing" (see page 13 of slip opinion), thereby embodying a frame of reference to which such absolute divining rod simply cannot be applied. As we have previously pointed out, the absence of such a legal obligation is of "minimal significance".

See *Gordon v. Commissioner*, 85 T.C. 309, 331 n.16 (1985).

We are particularly unimpressed by petitioner's reliance on *Estate of Cristofani v. Commissioner*, 97 T.C. 74 (1991), a case which petitioner apparently did not previously consider relevant and therefore failed to cite in his original or reply brief. In point of fact, *Estate of Cristofani* is clearly distinguishable. There, we found "no agreement or understanding between the decedent, the trustee and the beneficiaries that decedent's grandchildren would not exercise their withdrawal rights". *Estate of Cristofani v. Commissioner*, 97 T.C. at 77. In this case, we specifically concluded that there was an agreement or understanding that Nancy, Meredith, and Permenter would utilize the cash received from petitioner to participate in the bond transactions and acquire the interests remaining after the life interests in accordance with the expectations of the parties. (See page 8 of slip opinion.) In any event, petitioner, who has the burden of proof (see page 8 of slip opinion), has failed to persuade us that he did not acquire "the entire ownership in the bonds and then divided that ownership by retaining a life interest and transferring the remaining interests to Nancy, Meredith, and Permenter." (See page 12 of slip opinion)

/s/ Theodore Tannenwald, Jr.
Judge

Dated: Washington, D. C.
November 18, 1996

APPENDIX 3 — OPINION OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT DECIDED MARCH 3, 1998

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

JULIAN P. KORNFELD,
Petitioner-Appellant,

v. No. 96-9016

COMMISSIONER OF
INTERNAL REVENUE,
Respondent-Appellee.

APPEAL FROM THE UNITED STATES TAX COURT
(T.C. NO. 13169-95)

Submitted on the briefs:

Tom M. Moore and Clarke L. Randall of Kornfeld Franklin Renegar & Randall, Oklahoma City, Oklahoma, for Petitioner-Appellant.

Richard Farber and Thomas J. Sawyer, Attorneys, Tax Division, Department of Justice, Washington, D. C., for Respondent-Appellee.

Before SEYMOUR, Chief Judge, LOGAN and MURPHY, Circuit Judges.

LOGAN, Circuit Judge.

This appeal presents the question whether the Tax Court correctly relied on the substance over form doctrine in determining that Julian P. Kornfeld (taxpayer) was not entitled to a federal income tax deduction for amortization of a life interest in bonds that he purportedly jointly purchased with his daughters and secretary, who took remainder interests.

> The legal right of a taxpayer to decrease the amount of what otherwise would be his taxes, or altogether avoid them, by means which the law permits, cannot be doubted.... But the question for determination is whether what was done, apart from the tax motive, was the thing which the statute intended.

Gregory v. Helvering, 293 U.S. 465, 469 (1935).[1]

I

When a taxpayer purchases a bond the normal rule is that the security is not depreciable or amortizable for federal

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[1] After examining the briefs and appellate record, this panel has determined unanimously to grant the parties' request for a decision on the briefs without oral argument. See Fed. R. App. P. 34(f); 10th Cir. R. 34.1.9. The case is therefore ordered submitted without oral argument.

income tax purposes.[2] 5 J. Mertens, Law of Federal Income Taxation § 23A.93 (1990). Instead the taxpayer has a cost basis in the bond and when the bond matures or is called or sold the money received is treated as a nontaxable return of capital to the extent of that basis. The interest paid while the taxpayer holds the bond is taxable income unless, as here, it is tax exempt. See Internal Revenue Code (IRC) § 1001. If the taxpayer owns the bond at his death its value is included in his estate for federal estate tax purposes. Id. § 2033. If during his lifetime he should transfer ownership of the bond by gift reserving income for his life the entire value of the bond would still be included in his estate for federal estate tax purposes. Id. § 2036. Additionally, because the gift would be of a future interest the $10,000 per donee annual gift tax exclusion of IRC § 2503(b) would not apply.

Taxpayer, an experienced tax attorney, apparently believed he found a way to structure purchases of tax-exempt bonds to give him other income and estate and gift tax benefits. His method was to enter into agreements (through a revocable trust he created) with his daughters, Nancy and Meredith, to jointly purchase the bonds with taxpayer buying a life estate and his daughters buying the remainder interests in the following manner: Taxpayer ordered bonds from Prudential-Bache Securities Inc. which billed his trust. Under the agreements with the remaindermen taxpayer determined the value of his life estate based on Internal Revenue Service (IRS) estate and gift tax actuarial tables. Taxpayer's trust paid Prudential-Bache the value of his life estate interests. Taxpayer contemporaneously sent checks to his daughters in the amount of the purchase price

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[2] In the case of a taxable--not a tax-exempt--bond, the amount of the amortizable bond premium for the tax year may be allowed as a deduction. IRC §171.

of their shares. The daughters would then pay Prudential-Bache for the sum representing their remainder interests.[3]

After taxpayer executed two agreements, Congress amended the Code to provide that "[n]o depreciation deduction shall be allowed ... to the taxpayer for any term interest in property for any period during which the remainder interest in such property is held (directly or indirectly) by a related person." IRC § 167(e). A "term interest in property" is defined to include a life estate, and "related persons" includes taxpayers' children. Id. §§ 167(e), 267, 1001(e)(2). Taxpayer modified the later agreements so that rather than purchase the entire remainder interest Nancy would purchase a second life estate to take effect after taxpayer's death; taxpayer's secretary, Patsy Permenter, purchased the final remainder interest with funds given her by taxpayer. Taxpayer reported the gifts to Nancy, Meredith and Permenter on belatedly filed gift tax returns, claiming the $10,000 annual exclusion for each donee and using

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[3]After the first transaction taxpayer became concerned about his daughter Meredith's precarious financial situation and he did not want her interests to be attached by her creditors. Thus the second, third and fourth agreements included Nancy but not Meredith.

The bonds apparently were held in street name with no indication of the division of ownership between the life tenant and the remaindermen. The agreements also provided that evidence of ownership "may also be held by the First Interstate Bank of Oklahoma, as custodian" in such names or forms "as the custodian shall deem appropriate and convenient." Ex. 4-D. The parties agreed to sell, assign, or pledge only on joint direction of all parties, and to give to each other a right of first refusal at the valuations established by the IRS regulations in the event any one sought to dispose of his or her interest.

his lifetime exemption (unified credit) to avoid paying any tax. See IRC §§ 2010 and 2505. The tax-exempt bonds at issue here had a combined face value of $1,510,000. The actuarial value of taxpayer's life estate based on IRS tables was about $1,262,000.

We have only an income tax question before us. Taxpayer's federal income tax returns for the years 1990 and 1991 reflected tax-exempt interest income on the bonds of $118,972 and $122,974, respectively. Taxpayer also claimed an amortization deduction on his life estate in the bonds of $56,203.94 for each year. After an audit the Commissioner disallowed the amortization deductions. Taxpayer petitioned the Tax Court for a redetermination of the deficiency and before trial the parties stipulated to the facts and presented the case on that fully stipulated record.

Relying on the substance over form doctrine, the Tax Court found that the taxpayer had acquired the entire ownership interest in the bonds and then made a gift of the remainder interests to his daughters and Permenter. Thus, the Tax Court upheld the Commissioner's determination that taxpayer was liable for income tax deficiencies of $11,803 for 1990 and $13,122 for 1991.

II

Taxpayer first asserts that we must review the Tax Court's decision de novo because the parties submitted the case to the Tax Court on a fully stipulated record, citing *ABC Rentals of San Antonio, Inc. v. Commissioner of Internal Revenue*, 97 F.3d 392 (10th Cir. 1996). In *ABC Rentals*, we stated that "given the stipulated facts, the question of whether the [rental] inventory fits into the exception [] presents a legal issue regarding application and interpretation of [the applicable

statute]," 97 F.3d at 395. We went on to note, however, that even if the facts had not been stipulated, that case presented "a mixed question of law and fact in which the legal issues predominate." Id. at 395-96. In contrast, in a case involving whether a transfer of contract rights was genuine, we said that findings "as to what is substance in a transaction are to be treated as questions of fact," *Wisebart v. Commissioner*, 564 F.2d 34, 37 (10th Cir. 1977), and thus reviewed under the clearly erroneous standard. See *Anderson v. City of Bessemer*, 470 U.S. 564, 574 (1985) ("Where there are two permissible views of the evidence that the factfinder's choice between them cannot be clearly erroneous.... This is so even when the district court's findings do not rest on credibility determinations, but are based instead on physical or documentary evidence or inferences from other facts."). In the instant case, although the facts were stipulated, the Tax Court was still charged with making ultimate findings of fact as to the substance of the transaction. We do not need to determine which standard of review is applicable here, however, because under either standard we hold the Tax Court correctly disallowed the amortization deduction.

III

The taxation scheme set out in the Internal Revenue Code is complicated and the tax consequences of many transactions depend on form, how the transaction is structured. At the same time it has long been held that "[t]he incidence of taxation depends upon the substance of a transaction.... To permit the true nature of a transaction to be disguised by mere formalisms, which exist solely to alter tax liabilities, would seriously impair the effective administration of the tax policies of Congress." *Commissioner v. Court Holding Co.*, 324 U.S. 331, 334 (1945). Ascertaining the "true nature" of the transaction while adhering to neutral principles of statutory construction is often difficult. That is exemplified by the instant

case, in which the Tax Court opinion and the two others closest factually--one relied on by taxpayer and the other by the Commissioner--were authored by the same judge. Compare *Gordon v. Commissioner*, 85 T.C. 309 (1985) (where taxpayer gave family trust funds to purchase remainder interests in bonds for which he purchased a life estate, and claimed amortization deduction, Tax Court determined that in substance taxpayer purchased the bonds and gave remainder to trust) with *Richard Hansen Land, Inc.*, 65 T.C.M. (CCH) 2869 (1993) (distinguishing *Gordon* because although corporation was source of funds for shareholders' purchase of remainder interests, the corporation that purchased a term interest did not use shareholders' bank accounts as "mere stopping place" for funds).

There would be no doubt of taxpayer's right to annual amortization deductions had he acquired only a limited interest in the bonds in arm's length commercial transactions in which the remainder interests had been retained, or independently acquired, by persons having no connection to taxpayer. A taxpayer may amortize a limited interest in property if the "intangible asset is known from experience or other factors to be of use in the ... production of income for only a limited period, the length of which can be estimated with reasonable accuracy." Treas. Reg. § 1.167(a)-3. Here, however, one hundred percent ownership of the bonds was acquired from or through Prudential-Bache in a market transaction; but taxpayer presented no evidence that any brokerage firm would sell only a life estate in the bonds. The division of the interests between taxpayer's life estate and the remainders was made by the separate agreements between taxpayer and his daughters and secretary; the valuations were not determined by market forces but in accordance with IRS valuation tables formulated for estate and gift tax purposes. The broker sent one bill to taxpayer's trust, and taxpayer calculated the respective shares based on the IRS

tables, and then immediately gave the remaindermen gifts of nearly the exact amounts they needed to pay their shares. The parties stipulated that "[t]he purpose of these [gift] checks was to provide Meredith and Nancy with sufficient monies to pay their respective proportionate shares of the purchase price." Doc. 14 at 7.

Taxpayer tries to focus the question before us on the cash nature of the gifts to the daughters and secretary. He argues that they had sufficient independent assets to make their proportionate payments, and that they were not legally obligated to use the money gifted to them to make the payments for which they were obligated under their agreements. Thus he would have the court treat the gifts as separate from the purchases of the bonds, and he would have the court regard the remainder purchases in the bonds as independent investor decisions.

The government has applied, and the Supreme Court expressly sanctioned, a step-transaction doctrine to deal with purportedly separate transactions that the government believes should be treated as integrated. See *Commissioner v. Clark*, 489 U.S. 726, 738 (1989). "Under this doctrine, interrelated yet formally distinct steps in an integrated transaction may not be considered independently of the overall transaction. by thus linking together all interdependent steps with legal or business significance, rather than taking them in isolation, federal tax liability may be based on a realistic view of the entire transaction." Id. (quotation and citation omitted). In *Associated Wholesale Grocers, Inc. v. United States*, 927 F.2d 1517 (10th Cir. 1991), we identified three step transaction tests: "end result," "interdependence," and "binding commitment."

Taxpayer essentially argues that the facts here meet the "binding commitment" test because his daughters and secretary were not legally obligated to use his gifts to purchase the bonds.

But in *Associated Wholesale Grocers* we stated that this test is seldom applied. See id. at 1522 n.6. We thus examine the facts under the other step transaction tests. The "end result" test amalgamates into a single transaction separate events which appear to be component parts of something undertaken to reach a particular result. Id. at 1523. The instant case would appear clearly to satisfy the "end result" test. The "interdependence test" focuses on the relationship between the steps, whether under a reasonably objective view the steps were so interdependent that the legal relations created by one of the transactions seem fruitless without completion of the series. Id. Although the gifts here could stand on their own without relation to the investments, it is difficult to conceive that the parties would have made the investments as they did, or that they would have agreed to the valuations between life estates and remainders, in the absence of the gifts taxpayer made. Thus this case would seem to satisfy the "interdependence" test.

We conclude that the Tax Court properly characterized the transactions in the instant case as impermissible attempts to create amortizable term interests out of nondepreciable property. We agree with the *Gordon* opinion that "it is important to note that what is involved in this case is a simultaneous joint acquisition of income interests and remainder interests where the consideration moved to a third party who was not in any way concerned with the arrangements between the joint acquirers....[and that] it is appropriate to take into account the fact that the participation of the acquirer of the remainder interest is an essential element in affording the acquirer of the income interest the opportunity to obtain the tax benefit of an amortization deduction." 85 T.C. at 325.

We also agree with the *Gordon* opinion that where, as here, the "parties to the transactions in question are related, the level of skepticism as to the form of the transaction is

heightened, because of the greater potential for complicity between related parties in arranging their affairs in a manner devoid of legitimate motivations." Id. (quotation and citation omitted).[4] Complicity among the parties is further supported by the following: the parties established their respective purchase obligations by IRS tables that are only periodically adjusted and which reflect market values only in a general way; the parties committed to acting jointly in disposing of their interests, agreeing that if one wanted to sell he or she must offer to the others at the IRS table valuations; and that there is no external manifestation of their separate ownerships (as would be the case of recorded real estate deeds specifying term interests) to permit marketing of a limited interest to outside parties. Cf. *Schultz v. United States*, 493 F.2d 1225 (4th Cir. 1974) (brothers' gifts of shares in closely held corporation to each other's children were reciprocal transactions made to enlarge gifts to own children and thus gift tax exclusion was properly disallowed).

Finally, although there was no legal requirement that remaindermen would use the gifts of money to purchase the bonds, taxpayer stipulated that his intention in making the gifts was to enable the donees to make the purchases. We question the financial capacity of at least some donees, noting taxpayer ceased making daughter Meredith a party for fear her creditors might attach her interests. And there is no reason these remaindermen would question making the investments when taxpayer was giving them the funds to make their purchases.

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[4] Although Permenter is not a natural object of taxpayer's bounty in the same sense as his daughters, she is his long time secretary, cotrustee of his revocable trust, and taxpayer made contemporaneous gifts to her to enable the purchases of her remainder interests. In such circumstances it is not inappropriate to treat her in the same category as a related party.

Expressed colloquially, one does not look a gift horse in the mouth.

AFFIRMED.

APPENDIX 4 — ORDER OF THE UNITED STATES COURT OF APPEALS FOR THE TENTH CIRCUIT DENYING MOTION FOR REHEARING DATED APRIL 27, 1998

UNITED STATES COURT OF APPEALS
FOR THE TENTH CIRCUIT

JULIAN P. KORNFELD,
Petition-Appellant,

v. No. 96-9016

COMMISSIONER OF
INTERNAL REVENUE,
Respondent-Appellee.

ORDER
Filed April 27, 1998

Before **SEYMOUR,** Chief Judge, **LOGAN,** and **MURPHY,** Circuit Judges

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Julian P. Kornfeld's petition for rehearing is denied.

The suggestion for rehearing en banc was transmitted to all of the judges of the court who are in regular active service as required by Fed. R. App. P. 35. As no member of the panel and no judge in regular active service on the court requested that the court be polled, the suggestion is also denied.

Entered for the Court
PATRICK FISHER, Clerk of Court
By /s/ L. Balzano
Deputy Clerk

FILED
FILED
SEP 2 1998
OFFICE OF THE CLERK
SUPREME COURT, U.S.

No. 98-110

In The

Supreme Court of the United States

October Term, 1998

JULIAN P. KORNFELD,

Petitioner

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent

On Petition for Writ of Certiorari to the United States Court of Appeals for the Tenth Circuit

SUPPLEMENTAL BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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Attorney for Petitioner

SUPPLEMENTAL BRIEF

Pursuant to Rule 15.8 of the Supreme Court Rules, Petitioner respectfully submits this Supplemental Brief in support of his Petition for Certiorari, in order to bring to the attention of the Court the decision of the United States Court of Appeals for the Second Circuit in *Jonathan P. Wolff v. Commissioner of Internal Revenue,* 148 F.3d 186 (hereinafter "*Wolff*")".

SUMMARY OF ARGUMENT

The mere fact that a taxpayer selects a method for a transaction in order to achieve more favorable tax consequences does not justify the imposition of the legal "substance over form" fiction.

ARGUMENT

The *Wolff* case involved the question of whether recognized losses from the cancellation of forward contracts were ordinary losses (as contended by the taxpayer) or capital losses (as contended by the Commissioner).[1]

Forward contracts (a form of commodity futures contracts) could be canceled either by "offset" (which

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[1]Under the law in effect for the years involved, an ordinary loss was fully deductible against income of any nature; whereas a capital loss was only deductible against capital gains and a limited amount of other types of income.

conceedly produced a capital loss) or by "cancellation and termination" which, as argued by the taxpayer, produced an ordinary loss. The mechanics of the "offset" and "cancellation and termination" were different in form as well as substance.

Notwithstanding that at the time of the Tax Court's decision, the United States Court of Appeals for the D.C. Circuit had decided the identical issue in favor of the taxpayer[2] in *Stoller v. Commissioner*, 994 F.2d 855 (D.C. Cir. 1993), amended by 3 F.3rd 1576 (per curium), the Tax Court held for the Commissioner because the "economic result" is the same whether the forward contract is closed by offset or cancellation.

The Second Circuit disagreed, stating:

> "By applying the *Covington* analysis to a contract cancellation, the Tax Court majority would have us impose the legal fiction that, although the contract was canceled, it should nonetheless be treated as if a new offsetting contract was obtained and the two offsetting contracts continued to exist until the settlement date, when delivery of the underlying commodities or securities would be 'deemed' to occur. At that point, the

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[2] The taxpayer in *Stoller* was a member of the very same partnership as the taxpayer in *Wolff*.

> 'sale or exchange' requirement of §1222 would be deemed to have been met under the *Covington* analysis. As Judge Halpern noted in his dissent, this theory 'is not reality; it is a fiction built upon a fiction,' and it is a 'drastic extension of the doctrine of substance over form'." 148 F.3d at 189 (Emphasis supplied)

The Second Circuit further made clear that a taxpayer may choose an alternative method of accomplishing a transaction to obtain more favorable tax consequences stating:

> "Although the economic result achieved by offset or cancellation is identical, both the form and substance of the two closure methods are materially different. The mere fact that Holly [taxpayer] selected the cancellation method in order to achieve more favorable tax consequences does not justify imposition of the legal 'substance over form' fiction. That doctrine applies if the form of a transaction does not accurately reflect its true substance, which is not the case with respect to the Holly contracts." 148 F.3d, at 189 (Emphasis supplied)

Similarly, in the case before this Court, the Tax Court and the Tenth Circuit created a fiction that Julian purchased 100% of certain bonds and then transferred a remainder interest in the bonds to his children and secretary. However, the stipulated facts were that Julian made cash gifts to his two children and secretary; they deposited the cash gifts to their own separate accounts; and then wrote their own separate checks on their own separate bank accounts to Prudential Securities for their remainder interest in the bonds. From an economic standpoint, Julian ends up with a life estate in the bonds and his children and secretary end up with a remainder interest in the bonds. But, the means by which the end result is accomplished are totally different. The Tax Court's and the Tenth Circuit's conclusions that Julian bought 100% of the bonds and gave remainder interests to his children are based upon a total fiction and ignore the stipulated facts in this case.

CONCLUSION

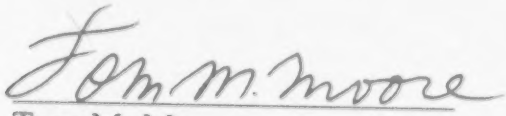
The substance and form of the transaction in this case are the same. This Court should not allow the Tax Court and the Tenth Circuit to create a fiction upon which to create a greater amount of tax for the government. As Judge Halpern stated in his Tax Court dissent:

> "I dissent because I believe that the majority is not justified in disregarding the actual transactions engaged in by Holly (the partnership) in favor of hypothetical transactions that yield the largest tax for the

Government." 108 T.C. 208 (1997), at 232.

Similarly, neither the Tax Court nor Tenth Circuit is justified in disregarding the actual transaction (gifts of cash to donees followed by deposits by donees into their separate bank accounts followed by donees' separate checks written to Prudential Securities for their remainder interests in bonds) in favor of hypothetical transactions (a purchase of 100% of the bonds by Julian followed by a gift of a remainder interest in bonds) that yield the largest tax for the government.

Respectfully submitted,



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